STATE OF CALIFORNIA GRAY DAVIS, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

September 30, 2002 Agenda ID #1159

TO: PARTIES OF RECORD IN RULEMAKING 92-03-050

This is the proposed decision of Administrative Law Judge (ALJ) Patrick, previously designated as the principal hearing officer in this proceeding. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. This matter was categorized as ratesetting and is subject to Pub. Util. Code § 1701.3(c). Pursuant to Resolution ALJ-180, a Ratesetting Deliberative Meeting to consider this matter may be held upon the request of any Commissioner. If that occurs, the Commission will prepare and mail an agenda for the Ratesetting Deliberative Meeting 10 days before hand, and will advise the parties of this fact, and of the related ex parte communications prohibition period.

The Commission may act at the regular meeting, or it may postpone action until later. If action is postponed, the Commission will announce whether and when there will be a further prohibition on communications.

When the Commission acts on the proposed decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the proposed decision as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's website at http://www.cpuc.ca.gov. Pursuant to Rule 77.3 opening comments shall not exceed 15 pages. Finally, comments must be served separately on the ALJ and the assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service.

/s/ CAROL A. BROWN
Carol A. Brown, Interim Chief
Administrative Law Judge

CAB:sid

Decision **PROPOSED DECISION OF ALJ PATRICK (Mailed 9/30/2002)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the Commission's Own Motion to Consider the Line Extension Rules of Electric and Gas Utilities.	Rulemaking 92-03-050 (Filed March 31, 1992)

(See Appendix A for a list of appearances.)

OPINION ON PROPOSED FREE INSPECTIONS AND ACCOUNTING CHANGES FOR LINE EXTENSIONS

I. Summary

This decision addresses further proposed changes to the Line Extension Rules governing the extension of gas and electric service to new customers. In today's decision, we conclude that since competition in utility line extensions is increasing, the proposed changes to the rules addressed in this phase of the proceeding are not needed. (1) For applicant-installed projects, we reject a proposal to provide free inspections at ratepayer expense; (2) for utility-installed projects, we reject an accounting change proposal to charge or credit utility shareholders the difference between the utility's bid amount and the utility's finished cost; and (3) for applicant-installed projects, we reject an accounting change proposal that would require the utility to book to ratebase the lower of the utility's bid amount or the applicant's cost.

We, also conclude that the inspection payments by applicants for applicant-installed projects, currently held in memorandum accounts by the utilities, should be credited to the utilities' plant-in-service accounts to reduce ratebase.

With this decision, the proceeding is closed.

II. Procedural Summary

Following several prehearing conferences, rulings by the assigned administrative law judge (ALJ), and an assigned Commissioner's ruling dated June 11, 2001, hearings on the issues remaining in this proceeding were held on January 22 and 23, 2002. This matter was submitted for decision on May 2, 2002, following the filing of briefs.

Opening and reply briefs were filed by Pacific Gas and Electric Company (PG&E), Southern California Gas Company (SoCalGas), San Diego Gas & Electric Company (SDG&E), and Southern California Edison Company (SCE), collectively referred to as Joint Utility Respondents (JUR), the California Building Industry Association (CBIA), The Utility Reform Network and Utility Consumers' Action Network (TURN/UCAN), and Utility Services Group (USG).[1]

III. Statement of the Case

The issues decided today arise from two earlier decisions. First, in Decision (D.) 99-06-079, the Commission, among other things, allowed applicants who selected the applicant-installed option a "first inspection of each section of

[1] USG comprises Utility Design, Inc. (UDI), Utility Service & Electric, and Pacific Utility Installation.

trench of their projects at no charge to the applicant." The related issue we address now concerns cost responsibility when the utility inspects applicant-installed work. Second, in D.97-12-099, the Commission included what has come to be known as "Paragraph 2," which purported to address accounting changes related to the applicant design process. That decision spawned the last two issues in this case relating to accounting for line extension costs.

IV. The Free Inspection Issue

When the Commission decided in 1985 to allow applicant installation of line extension facilities, it specifically adopted the principle that the applicant should bear the costs imposed on the utility to inspect the applicant's work. Accordingly, the utilities implemented a non-refundable inspection fee requirement paid by the applicant to cover the incremental cost of inspection (D.85-08-045). Subsequently, in D.99-06-079, the Commission decided to allow a first inspection of each section of trench at no charge to the applicants on applicant-installed projects. The Commission stated:

> "Our concern is that an applicant who chooses applicant-installation is required to pay additional inspection charges that the applicant who chooses utility-installation would not pay. This does not provide a level playing field. Therefore, we will adopt UDI's recommendation that applicant-installed projects be allowed one inspection at no charge for each section of trench; additional inspections of previously inspected sections of trench would be charged to the applicant. As pointed out by CBIA, one free inspection puts the competitor on an equal basis with the utility." (D.99-06-079, mimeo., p. 15.)

That decision generated related subsequent pleadings. UDI, on July 23, 1999, filed a petition to modify, arguing that the phrase "each section of trench" was ambiguous. On July 26, 1999, the JUR applied for rehearing, asserting legal

error in the decision and requesting a stay of the order. The Commission on September 2, 1999, stayed the order, and directed the JUR to set up tracking and memorandum accounts for the disputed charges. On January 6, 2000, the Commission denied the JUR petition for rehearing as a matter of law, but noted that petitions for modifications were the appropriate mechanisms to raise policy and clarification questions, as UDI had done in regard to this order. Accordingly, the JUR, on April 5, 2000, filed a petition for modification challenging the decision favoring a "free" first inspection on the policy ground that it increased costs to ratepayers. Since there was an insufficient record to address the petitions, at the ALJ's direction prepared testimony was provided by the parties and an evidentiary hearing held. Today's decision reflects the augmented record.

A. Positions of the Parties

The JUR take the position that applicants should continue to pay for the incremental cost associated with inspecting applicant-installed facilities rather than ratepayers and therefore no change in existing practices should be adopted. USG proposes to shift to ratepayers the incremental applicant-installed inspection costs to create a level playing field. Likewise, CBIA believes that applicant-installed inspection costs are an expense properly borne by ratepayers. TURN/UCAN would allow inspection fees to become part of the job costs subject to allowances, but only if TURN/UCAN's proposed accounting change is adopted to require the utilities to use the applicant's reported cost, or the utility's estimate, whichever is lower, for purposes of recording line extensions to rate base for applicant-installed jobs. If the Commission does not adopt TURN/UCAN's accounting proposal for applicant-installed jobs, TURN/UCAN

agree with the JUR that applicants should bear the full incremental cost associated with the inspection of applicant-installed facilities.

B. Discussion

While the requirement in D.99-06-079 that the utilities allow one inspection at no charge for each section of trench may seem simple on its face, there are problems with its implementation.[2] In sum, the testimony is that there is no workable definition of what would constitute such an inspection. For that reason alone, we are persuaded that the free inspection requirement should be dropped, notwithstanding the policy considerations we discuss below that dictate against charging these costs to ratepayers.

It is uncontroverted that applicant-installed line extensions cause incremental cost for inspection that are not incurred when the utility performs the work. When the utility performs the work, the utility foreman is charged

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[2] SoCalGas witness Frank Galvery testified that the term "section of trench" is ambiguous, it could mean that in some situations each street could be viewed as a section, it could mean a specific time period or refer to each utility operation, or it could refer to the joints at the ends of each 1,000-foot roll of plastic pipe used for gas lines.

SCE witness Mathew Deathrage testified that SCE was unclear as to what a "section" meant. He stated that a section does not necessarily mean a structure-to-structure type termination, but instead could mean certain footage or a block.

PG&E witness Parker testified that PG&E does provide applicants with a free inspection of the trench; however, there is confusion whether the free inspection would apply to facilities. Also, according to Parker, it would be a "logistical nightmare" to define a "first inspection" since inspectors often re-inspect work that did not pass, at the same time as they inspect new work. Thus, there would be controversy regarding the allocation of the inspectors' time.

SDG&E witness David Dohren testified that there was uncertainty whether the free inspection applied to the trench or the facilities.

with ensuring that the work conforms to all governmental and utility codes, ordinances and standards, and inspection is integrated into the construction process. On the other hand, when applicants elect to perform the work, and a non-utility contractor performs the construction, the utility has no choice but to inspect the work to ensure that the public is protected from unsafe conditions resulting from improperly installed facilities, and ratepayers are protected from the maintenance costs that would flow from defectively installed facilities. Since applicant-installed line extensions cause incremental costs the question is whether the applicants or ratepayers should be responsible for these costs.

The Commission has a long history of matching cost with cost causers in the line extension area. When the Commission decided to allow applicant installation of line extension facilities in 1985, it specifically ordered that the applicants "shall pay to the Utility, as a non-refundable amount, the cost of inspection." (D.85-08-045.) This provision of the decision is consistent with the Commission's later-stated policy of assigning costs to the party who causes the costs. In other words, the applicant is free to choose a third-party installer if it has a business reason to do so, but it must absorb the additional costs of inspection associated with that decision. Also, see D.94-12-026, mimeo., p. 2; and D.97-12-098, mimeo., p. 1; where the Commission affirms its policy that applicants should pay all costs associated with their projects that are not revenue justified.

However, in 1999, when the Commission decided to create a "level playing field" to promote competition by allowing applicant installers one free inspection for each section of trench (D.99-06-079), the Commission did not address the cost burden and whether ratepayers should pay for the cost of

inspections not supported by expected revenues, contrary to D.94-12-026. That is the issue now before us.

We keep in mind that applicants already receive a subsidy from ratepayers in the form of allowances and refunds for costs that are supported by expected revenues. Free inspections would create an additional subsidy of new construction projects at ratepayer expense in the name of creating more opportunities for third-party installers. Therefore, the question is whether there is a public policy reason for requiring ratepayers to assume these costs. We say "No" and affirm the Commission's long standing policy of requiring applicants for line extensions, whether utility installed or applicant installed, to pay for all costs that are not revenue justified consistent with D.85-08-045 and D.99-06-079.

As the testimony shows, for developers, whether to select utility installation or applicant installation is a business decision. The additional cost of utility inspections does not drive the developers' decision regarding applicant installation. Rather, developers are primarily concerned with timing, control, and scheduling of their project.

Moreover, as pointed out by the JUR, third-party installers are able to compete against the utilities with advantages that utilities cannot offer. Unlike utilities, private contractors can vary the terms of their contracts, adjust their profit margin, offer progress payments, and are not subject to being taken off a job in the event of a system emergency. These are all factors that help a private contractor to compete for a project.[3] Thus, the incremental cost of inspection of

[3] In contrast, the utilities require up-front payment of their estimated cost less allowances before undertaking a project.

applicant-installed facilities does not ultimately determine whether the utility or the applicant installs the facility. While we would like to see more applicant installations by third-party contractors in SCE's and SDG&E's service areas, the evidence in this proceeding is that competition in applicant installations is increasing; therefore, we are not persuaded that extraordinary measures to promote competition are warranted.[4]

In summary, we decline to shift the cost of first inspections of applicant-performed line extension work from applicants to ratepayers. Shifting these costs to ratepayers would violate sound Commission policies of matching costs with cost causers and of charging ratepayers only with the revenue-justified costs of line extensions. Accordingly, we will modify D.99-06-079 to do away with free inspections. We will continue to hold applicants responsible for incremental inspection costs on applicant-installed projects, and dissolve the memorandum accounts[5] established under D.99-09-034 for such inspection charges.

C. USG's Flat Across-The-Board Fee Proposal

As an alternative to free inspections for each section of trench, USG proposes a flat rate fee to applicants in all instances, whether the line extension facilities are installed by the utility or by the applicant.

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[4] For residential subdivisions, installation of line extension jobs by applicants is as follows:

PG&E	70%
SCE	15%
SDG&E	10%

[5] There was $3.7 million recorded in these memorandum accounts as of May, 2001. This amount should be credited to the utilities' plant-in-service accounts to reduce ratebase.

We conclude that USG's proposal is fundamentally unfair to applicants who choose the utility to do the work because such applicants do not cause incremental inspection costs. Charging an applicant for a cost not incurred is fundamentally at odds with any notion of charging the cost to the cost causer. Since it is not consistent with cost causation principals and does not send proper price signals, USG's flat rate fee proposal is rejected.

V. The Accounting Issues[6]

In D.97-12-099, the Commission made permanent the option for an applicant to select a non-utility designer for a line extension project.[7] The Commission also apparently attempted to specify an accounting approach for the utilities to follow when the utilities bid on a design job. It wrote:

> "Additionally, we will require the utility to book to its accounts the utility's bid amount, whether the design was done by the utility or an applicant. If the utility's actual cost was more than the bid amount, the utility would write off the excess. If the cost was less than the bid, the utility would provide the applicant with a credit equal to the utility's bid amount less any appropriate charges such as for plan checking." (Mimeo. at 7.)

This requirement came to be called "Paragraph 2."

On April 27, 1998, SCE and PG&E filed a petition for clarification regarding that language. The Commission responded with D.99-06-047, in which it held that the record in D.97-12-079 was insufficient to address the necessity for,

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[6] The two accounting issues identified by the ALJ in his March 15, 2000 ruling are combined for purposes of this decision.

[7] Earlier, in D.95-12-013, the Commission had approved a 24-month pilot program to test the feasibility of an applicant design option.

or any changes to, utility accounting procedures. The Commission ordered the assigned ALJ to develop a record to address what accounting changes, if any, should be made in the context of the applicant design process.

D.99-06-047 gave rise to two petitions for modification. One was filed by the CBIA, which asked that the accounting treatment for applicant design also apply to applicant-installed projects. USG similarly petitioned for modification urging the same change as CBIA. By ALJ ruling, evidence was taken on the CBIA/USG proposal.

A. Proposed Accounting Treatment for Utility-Designed and Utility-Installed Line Extension Projects

Under USG's proposal, supported by CBIA, the utility's cost estimate would always be booked to ratebase, whether the utility's actual cost was above or below the utility's cost estimate. Thus, if the actual cost should exceed the estimated cost, utility shareholders would absorb the amount in excess of the estimate. If the actual cost is less than the estimate, utility shareholders would benefit by the difference between the actual cost and the estimated cost.

1. Position of USG

USG argues that its proposed accounting treatment is necessary to ensure that the utilities compete fairly with third-party contractors. According to USG, without such accounting treatment, the utilities would engage in anticompetitive behavior by making below cost bids to obtain the work, and then charging the ratepayers for the actual cost, even if major cost overruns occurred.

USG contends that for years the utilities have enjoyed an unfair advantage over applicant third-party contractors, because when the utilities design or construct a line extension, all their costs are paid for by ratepayers. On the other hand, when the applicant performs the design or installation, the

applicant only gets reimbursed the line extension allowances. USG submits that having ratepayers pay all of the utilities' line extension costs is simply wrong and creates an unfair incentive for the applicant to choose the utility for the work.

2. Position of CBIA

CBIA supports USG's accounting recommendation because CBIA believes that it would promote development of a more competitive market for applicant-design and installation services, with the expectation that the competitive discipline of the market for such services will inevitably lead to lower costs for line extension applicants and ratepayers alike. According to CBIA, its goal is for applicants to have the opportunity to make an unbiased election between "utility versus third-party" services without incurring unreasonable and unrealistic financial penalties or project delay.

3. Position of TURN/UCAN

TURN/UCAN do not take a position on USG's proposed accounting change for utility-installed line extensions. However, TURN/UCAN recommend that the Commission adopt outcomes that promote ratepayer interests. TURN/UCAN argue that rather than continue to embrace outcomes that serve to promote "competition" as a goal in itself, the Commission should only rely on competition when doing so serves to promote ratepayer interests.

4. Position of the JUR

The JUR oppose USG's proposal requiring shareholders to bear the risk or receive the benefits of the difference in the utility's bid and its actual cost when the utility installs the project. The JUR argue that USG's proposal seeks to transform utilities into profit-driven providers of line extension services by introducing financial risks and rewards into the bidding process.

According to the JUR, USG's proposal would incline utilities to bid higher than normal to ensure that shareholders are not exposed to financial risk. Further, the JUR contend that instead of providing a benefit, USG's proposal would drive up the cost of line extensions for applicants. Third-party contractors would be free to increase their bids to a level just below the utility's bid enabling the applicant-installer to both win the job and maximize profits, all at the expense of applicants and ratepayers.[8]

5. Discussion

The practical effect of USG's proposal would be to shift line extensions from the utility's regulated operations to a separate shareholder operation within the utility. This does not make sense. If the Commission wanted to create a truly competitive market and put shareholders at risk for line extension work, it would have to allow utilities to decide which projects they want to undertake and allow them to include a profit component for their work, with the ability to make up for past losses in strong markets as do the private contractors. It is inconsistent to require utilities to use accounting treatments similar to a private firm while at the same time requiring them to provide traditional cost-based construction of utility infrastructure upon request, especially for jobs that third-party contractors do not want. The private designers and installers cannot reasonably expect to have it both ways in the name of competition.

[8] The utilities are required to provide applicants with bids, which the applicants may then use to shop for lower bids from third-party contractors.

Even if one accepts that competition, in and of itself, is a legitimate goal, CBIA and USG have failed to show that this goal has not already been sufficiently achieved. As PG&E points out, competition for applicant installations in its territory is strong, with applicants selecting third parties to install electric facilities for approximately 70% of the residential subdivision projects. SDG&E and SCE similarly report steady growth in competitive installation. In contrast, USG and CBIA offer no evidence indicating that competition in applicant design and installation is suffering because of current accounting practices.

We now turn to USG's argument that when utilities design or construct a line extension all their costs are paid for by the ratepayers; but on the other hand, when the applicant performs the design or installation, the applicant only gets reimbursed the line extension allowance.

There are two fundamental errors with USG's argument. First, USG errs in its understanding as to who pays the cost of an installation. The principle which underlies the treatment of line extensions is that those line extension costs supported by a revenue-based allowance are paid for by ratepayers as part of the overall rates, while costs in excess of the revenue-based allowance are paid by developers. This principle applies to both utility-installed and applicant-installed projects. In a utility-installed project, the applicant pays the costs charged by the utility, minus the applicant allowance. In an applicant installation, the applicant pays the costs charged by a contractor (or the applicant's directly incurred costs), minus the applicant allowance. In addition, certain costs paid by the applicant, under both the utility-installed and an applicant-installed option, are subject to refund, if additional load is added to the

system. Other costs paid by the applicant (again true for both utility and applicant-installed projects) are not refundable.

Thus, looking simply at the question of who pays the cost, there is no distinction in treatment between a utility installation and an applicant installation. In both instances, the ratepayers pay a portion of the cost in the form of the applicant allowance. Moreover, in both instances, the applicant is qualified under Tariff Rule 15 to receive a refund as additional meters (load) are added to the system. As noted by SDG&E witness Dohren, "In the end, the utility adds to ratebase an amount equal to the refunds paid to the applicant, subject to the allowance. Any advances that are not refunded are converted to a permanent ratebase deduction to the benefit of ratepayers."

The second fundamental flaw in USG's argument is that USG seems to take issue with the fact that a utility is able to recover its costs while an applicant cannot. The utility cannot be compared to the applicant, because the utility fulfills a distinct function from that of the applicant in the line extension process. The applicant is only concerned with installing the necessary facilities to serve its development. In contrast, the utility is regulated, is obligated to undertake projects that third-party contractors reject, and is compelled under statute to make investments in the distribution grid.[9] Accordingly, given the requirement to serve, it is only reasonable that the utilities' recover their costs. The theory is that over time, the gains and losses offset each other; therefore, the net effect on ratebase resulting from the difference between the estimate and the actual cost, is minimal. That is how the current accounting system works and

[9] See Pub. Util. Code § 399.2.

there is no compelling reason to change it. For the reasons set forth above, we conclude that USG's accounting proposal should be rejected.

B. Proposed Accounting Treatment for Applicant-Designed and Applicant-Installed Line Extensions

TURN/UCAN seek to limit the addition to the utility's ratebase on applicant-installed projects to the lower of the utility's installation bid or the applicant's cost.[10]

1. Position of TURN/UCAN

TURN/UCAN argue that the Commission has treated line extensions as "competitive" because an applicant can choose someone other than the utility to install a line extension, yet the benefits of such competition are not shared with the utility's ratepayers. TURN/UCAN point out that if an applicant installs a line extension, the amount added to the utility's ratebase is the amount the utility estimated as its cost for performing the installation, regardless of whether the applicant's actual costs are far less. As TURN/UCAN characterize it, the utility wins either way: Either it performs the work and recovers its recorded costs, plus the return it has the opportunity to earn on its ratebase, or it does not perform the work, incurs no direct cost itself, but records to ratebase its estimated cost of performing the work (creating, again, the opportunity to earn a return on the recorded ratebase amount). TURN/UCAN also point out that the applicant can choose to avoid the risk of cost overruns by accepting the utility's bid, having the utility perform the installation, and assigning to the utility's

[10] On applicant-designed and applicant-installed projects, the utilities book to ratebase their bid amounts less allowances as a proxy for the actual cost.

ratepayers the risk of cost overruns. Alternatively, if the applicant receives a bid from a non-utility installer that offers cost savings, the applicant can choose the lower-cost route. TURN/UCAN contend that ratepayers bear entirely the risk of utility cost overruns, even to the extent that the overruns cause the utility's costs to exceed the revenue-based allowance, yet they receive none of the benefits of the potential cost savings from non-utility installations.

2. Position of CBIA

CBIA argues that while the current ratemaking treatment contemplates absolutely "zero" risk/reward for shareholders, the language set forth in Paragraph 2 of D.97-12-099, requiring the utility "to write off the excess" if actual costs exceed the bid amount, represents a clear Commission intention to include some element of shareholder risk/reward with respect to utility provision of line extensions. As CBIA perceives it, the Commission's ultimate interest in holding the utility accountable for the accuracy/validity of its cost estimates and in providing for shareholder incentives with respect to utility provision of line extension services is the promotion of competition and resulting reductions in utility extension costs. CBIA believes that, given the Commission's commitment to promote competition with respect to line extension services, a good starting point would be a requirement that the competitors, including the utilities, play by the same rules.

3. Position of the JUR

The JUR point out that the TURN/UCAN proposal assumes that one can accurately determine an applicant's cost and that the cost reported by the applicant is a fair measure of the value of the installed facilities. The JUR submit that neither assumption is accurate. The JUR witnesses say that neither the utility nor the Commission may compel an applicant to accurately or timely

report its final project cost. Thus, the JUR contend that under this proposal, the entire system of ratebase refunds, and allowances, would be based on the naive expectation that applicants will provide timely and accurate cost data.

Further, the JUR argue that, since there is currently no oversight of applicants, it is fair to anticipate that some applicants or applicant-installers will game the system if it is to their economic advantage. SCE, in its opening testimony, provided one example of where an applicant might report higher costs than were paid by the applicant to maximize the refundable amount. In other instances, as suggested by SoCalGas, an applicant might report an artificially lower amount to minimize its tax liability. In either situation, the utility would be compelled to record an amount that does not accurately reflect the value of the installation, thus distorting everything that flows from those cost numbers, including, but not limited to, the refundable amount and ratebase.

4. Discussion

As discussed above, TURN/UCAN propose that for applicant-performed work, the utility book to ratebase the lower of the utility estimated cost or the applicant's actual cost. The objective of the TURN/UCAN proposal is to reduce the amount booked to ratebase. However, as the amount now booked to ratebase for applicant-performed work is capped at allowances plus refunds, the utility's estimate has no impact on ratebase under current procedures. This is the practical result of the fact that most line extension work, particularly for subdivisions, is more expensive than the amount that would be supported by expected revenues, and the Commission has decided that the applicants should pay for line extension costs that exceed allowances. Because of this, ratepayers would not realize any savings from the TURN/UCAN proposal unless the applicant's actual cost came in not only under the utility's estimated cost, but

also under allowances. Moreover, as pointed out by the JUR, there is no evidence that third-party contractors can realistically perform the work for less than the allowances. Therefore, we believe that ratepayer benefits, if any, would not be significant.

TURN/UCAN assert that the utilities are exaggerating the administrative burden that the proposed accounting change would produce. They cite to the fact that in other contexts, utilities rely on verifications to establish eligibility for certain rate options. We do not find TURN/UCAN's argument persuasive. There is no comparability between the utilities' practice of establishing customer eligibility for certain rates, and TURN/UCAN's proposal to require utilities to gather and rely on cost data supplied by third-party contractors. Unlike the utilities' relationships with ongoing customers, the utilities do not have an ongoing relationship with the third-party designers and installers performing line extension work, and they have no practical means of verifying the data supplied, nor do they have any practical means of discovery or recourse if it is false. Most importantly, third-party installers have no incentive to provide accurate data, and they are not in privity of contract with the utilities.

On balance, we are not convinced that the proposed changes could actually produce ratepayer savings. Therefore, the TURN/UCAN proposal is rejected.

VI. Comments on and Proposed Decision

The proposed decision of the Administrative Law Judge (ALJ) in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure. Comments were filed on _____, and reply comments were filed on _____.

VII. Assignment of Proceeding

Henry Duque is the Assigned Commissioner and Bertram Patrick is the assigned ALJ in this proceeding.

Findings of Fact

1. There is increasing applicant installation and applicant design activity in California.

2. The utilities incur incremental inspection costs for inspecting applicant-installed facilities when the applicant performs the line extension installation.

3. In D.99-06-079, the Commission decided to create a level playing field to promote competition by allowing applicant installers one free inspection for each section of trench.

4. In D.99-06-079, the Commission did not address the issue of whether the ratepayers should be required to pay the incremental cost caused by the decision of the applicant to choose the applicant-installed option.

5. If the utilities were to stop their current practice of charging applicants' inspection fees, millions of dollars would be shifted from applicants to ratepayers.

6. Existing inspection fees provide the proper incentives to applicants to minimize utility inspection costs.

7. The USG accounting change proposal to place the utilities' shareholders at risk for the difference between actual cost and estimated cost when the utility does the work would likely cause the utilities to increase cost estimates in order to protect shareholders, thus providing the opportunity for third-party contractors to increase their bids to just under the utility's bid. This would not benefit applicants and ratepayers.

8. The TURN/UCAN accounting change proposal, to require the utilities to book the lower of the estimated cost or the applicant's reported cost when the applicant installs the line extension facilities, would increase the utilities' administrative costs borne by ratepayers and provide applicants with a strong incentive to provide inaccurate cost data to the utilities.

9. Ratepayers would not realize any savings from the TURN/UCAN accounting change proposal unless the applicants' actual cost came in not only under the utility's estimated cost, but also under allowances.

10. There is no evidence that for residential subdivisions, which constitute the bulk of the applicant-installed work, third-party contractors can perform the work for less than the allowances.

Conclusions of Law

1. Consistent with the Commission's policy of assigning costs to cost causers, the economic burden of incremental inspection costs caused by applicants electing to use third-party contractors should be assigned to these applicants.

2. The evidence in this proceeding is that competition in the line extension area is increasing; therefore, ratepayer subsidies are not necessary to encourage competition.

3. There is no public policy justification for requiring ratepayers to bear the cost of providing free inspections for applicant installations in order to promote competition for line extension work.

4. The incremental utility cost associated with inspecting applicant line extension installations should continue to be borne by the applicant because the applicant causes these costs to be incurred by the election to use a third-party contractor to install the line extension facilities.

5. Proponents of changes to existing utility accounting rules have not met their burden of proving that the proposed changes would generate ratepayer benefits sufficient to offset ratepayer costs.

6. The existing accounting for line extension costs is fair and reasonable and no cause has been shown to alter existing utility accounting practices.

7. The proposals for free inspections and utility accounting changes addressed herein should be rejected.

8. Today's order should be made effective immediately to resolve long-standing issues as soon as possible.

O R D E R

IT IS ORDERED that:

1. The proposal to provide free inspections at ratepayer expense for applicant-installed line extension projects is rejected, and Decision (D.) 99-06-079 is modified accordingly.

2. The memorandum accounts established by D.99-09-034 to track applicant-installation inspection fees are hereby terminated.

3. The proposal to change the utilities' accounting procedures to charge or credit utility shareholders the difference between the utilities' bid amounts and the finished costs for utility-installed projects, is rejected. D.97-12-099, Paragraph 2, is modified accordingly.

4. The proposal to change the utilities' accounting procedures to require the utilities to book to ratebase the lower of the utilities' bid amount or the applicants' costs for applicant-installed projects, is rejected.

5. This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.

Appendix A to R9203050 Patrick Comment Dec.